International Sovereign Energy Corp.

2001 Annual Report

Corporate Profile

International Sovereign Energy Corp. is a Canadian based publicly traded exploration and development company with offices in Calgary, Vancouver and Pakistan and is active in the exploration and development of hydrocarbon reserves in Western Canada and internationally.

The Company, incorporated in 1992, owns and operates a strong asset base of producing oil and gas properties in Western Canada that it continues to maintain through the drilling of internally generated low to medium risk exploration and development opportunities. This conservative, low risk approach to growth in Western Canada provides the Company with a substantial asset base from which to identify and pursue late stage exploration or early stage development opportunities internationally.

The Company is committed to maximizing shareholder value through the rapid growth expected through its international initiatives as well as to significantly increase its Western Canadian reserve base.

The shares of International Sovereign Energy Corp. are publicly traded on the Canadian Venture Exchange under the symbol "ISR". At year-end 2001, the Company had 6,445,313 shares issued and outstanding.

Annual Meeting

The Annual General Meeting of Shareholders of the Corporation will be held on Wednesday, June 12, 2002 at 2:30 p.m. in the Salon Pommard Room at the Sutton Place Hotel located at 845 Burrard St., Vancouver, British Columbia. Shareholders and members of the public who are interested in receiving additional information on the Company are encouraged to attend.

Contents

Abbreviations

ARTC	Alberta Royalty Tax Credit
bbl	barrel
bbls/d	barrels per day
bcf	billions of cubic feet
BOE	barrel of oil equivalent (1 bbl = 6 Mcf)
bopd	barrels of oil per day
BTU	British Thermal Unit
Mbbls	thousand barrels of oil
MBOE	thousand barrels of oil equivalent
Mcf	thousands of cubic feet
MMcf	millions of cubic feet
NGLs	natural gas liquids

Highlights – Year in Review

	2001	2000
Operating		
Production		
Oil & NGLs (bbls)	154,070	96,598
Per day	422	264
Natural Gas (Mcf)	217,421	273,693
Per day	596	748
Exit Production		
Oil & NGLs (bopd)	384	440
Natural Gas (Mcf per day)	532	840
Proven and Probable Reserves		
Oil & NGLs (Mbbls)	1,690	1,287
Natural Gas (MMcf)	6,361	4,327
Average Price Received		
Oil ($ per bbl)	21.29	32.20
Natural Gas ($ per Mcf)	5.74	5.83

	2001	2000
Financial		
Gross Revenue	$ 4,527,950	$ 4,706,765
Cash Flow	1,896,121	2,865,821
Per Share	0.29	0.44
Net Income (Loss)	445,220	1,121,270
Per Share	0.07	0.17
Capital Expenditures	1,562,240	2,428,478
Acquisitions	0.00	653,346
Divestitures	15,000	0.00
Long Term Debt	nil	nil
Net Asset Value (15% DCF)	16,918,709	15,219,475
Per Share	$ 2.63	$ 2.36
Class A Common Shares Issued at Year End	6,445,313	6,442,713

Lutfur Rahman Khan
Chairman of the Board

I am pleased to report to the Shareholders of International Sovereign Energy Corp. that the Company was again successful in showing growth on the key aspects of its business for the year ending December 31, 2001.

The Company's growth is reflected in a 31% increase in our oil and natural gas liquids reserves and a 47% increase in our natural gas reserves on a proved plus probable basis over the previous year. This was achieved through a modest capital expenditure on domestic operations of $994,000 which translates into the Company posting a reserve increase at a cost of $6.28/BOE.

The loss of 10 months of gas production from the Company's Clarke Lake property combined with record light-heavy oil differentials in the fourth quarter of 2001 stemming from downstream refining restrictions in the U.S., resulted in gross revenue of $4,528,000, a 4% decrease from the year prior. At the time of writing of this message, the pipeline repair has been completed and approximately 340 Mcf/d gas production was restored to the Company's account. As well, heavy oil prices recovered dramatically at the end of the first quarter, 2002.

The above events, combined with increased royalties and increased operating costs resulted in a 34% decrease in cash flow from the previous year. The Company successfully operated within its means without any dilution to our shareholders or increase in debt and increased the net asset value of the Company by 11%, which equates to $2.63 per share.

The Company's primary focus is to secure and develop world-class international oil projects which will provide rapid growth and extraordinary return on investment to our shareholders. Our ability to source and evaluate international opportunities relies on the strength of our Western Canadian asset base. Management is committed to maintaining the quality as well as increasing the production levels of its domestic operations.

With the cost of acquiring assets reaching unprecedented levels throughout the year, the Company focused its growth strategy toward internally developing low to medium risk drilling prospects, primarily gas, with the goal of bringing our product mix more into balance. The upcoming year will start to reflect the positive results of this effort.

With the mega mergers that have occurred within the industry in recent months, the Company is anticipating that hundreds of millions of dollars worth of quality assets will become available in the coming year and we will include this alternative as part of our growth strategy.

Management of the Company has devoted much of its time during the past year to the identification and evaluation of international opportunities. I am pleased to report that we have made significant progress in our target areas.

In central Asia, subsequent to year end, the Company signed a Memorandum of Understanding with the State Oil Company of the Azerbaijan Republic giving it exclusive rights to negotiate on the terms of a Production Sharing Agreement for the rehabilitation, exploration and development of the largest onshore block in the country which contains an estimated 219 million barrels of recoverable reserves, of which only a fraction has been produced to date.

In Pakistan, the Company maintains a field office and is continuing its efforts to acquire interests in certain producing and non-producing concessions in the Lower Indus Basin, while in Ecuador the Company has established a subsidiary and is pursuing specific projects which it has identified as having significant undeveloped reserve potential.

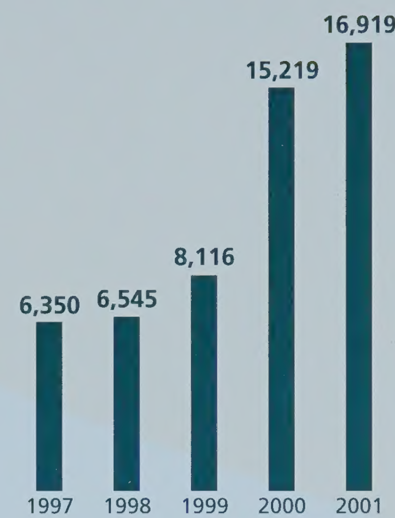
On behalf of the Board of Directors, I wish to thank our shareholders for their continued confidence and support and I look forward to reporting on the results of both our domestic and international efforts in the upcoming year.

Lutfur Rahman Khan
Chairman of the Board

April 24, 2002

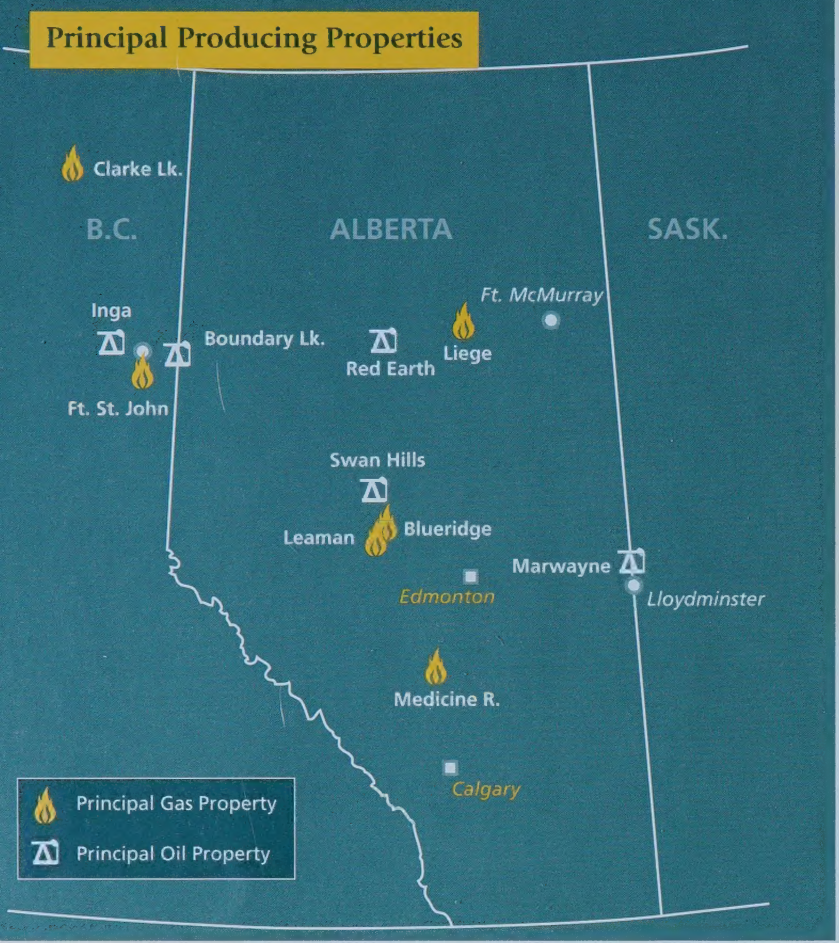
Net Asset Value

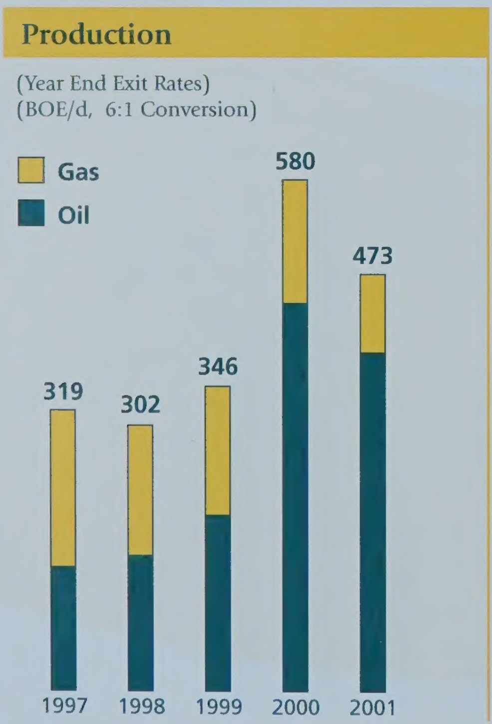
(15% DCF)
($ Thousands)



Cash Flow

($ Thousands)





Operations

International Sovereign drilled two successful 100% working interest wells on its Marwayne property late in the third quarter. The 12B-28-52-1W4M well came on production in the fourth quarter at 40 bopd from the GP sand. The 5C-28 well which was temporarily suspended prior to year end due to high sand cuts and low net backs for the oil is currently producing at approximately 25 bopd.

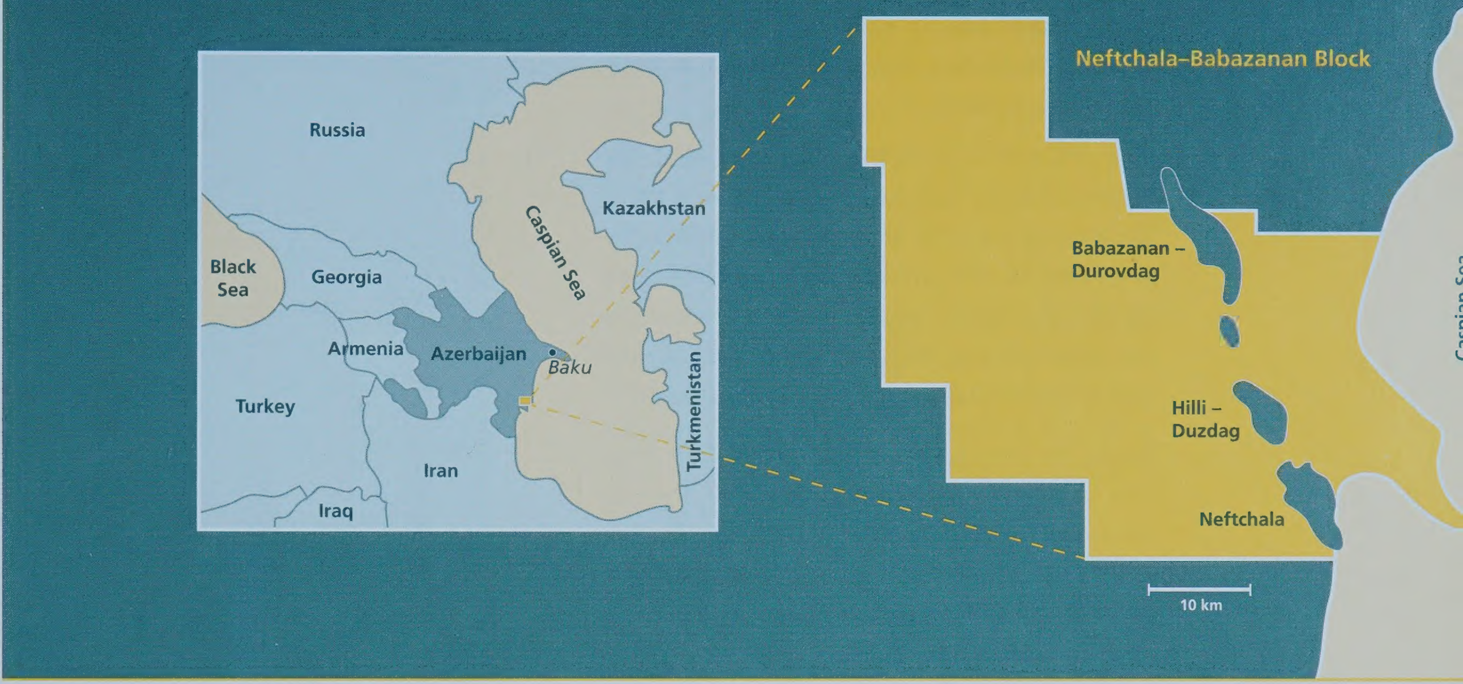
The Company participated as to a 50% working interest in a Bow Island sand test at Little Bow during the fourth quarter that was unsuccessful. Negotiations are underway to secure lands for additional drilling on the prospect.

Production

Average oil and NGLs production for the year increased 60% to 422 bopd while average gas production declined 20% to 596 Mcf/d as the result of the pipeline break at Clarke Lake. The decision to delay the work-over on the newly drilled 5C-28 location as well as to shut-in two additional wells at Marwayne at the end of November due to low commodity prices resulted in a year end exit rate for oil and NGLs of 384 bopd, down 13% from the previous year while the gas production exit rate was off 37% to 532 Mcf/d.

Subsequent to year-end, heavy oil prices recovered significantly and full production at Marwayne was restored to approximately 340 bopd. As well, the pipeline break at Clarke Lake was repaired and 340 Mcf/d gas production is expected to resume mid-April, 2002 resulting in production levels from existing properties increasing to approximately 650 BOE/d at that time.

Neftchala–Babazanan Block



Subsequent to year-end, the Company entered into a Memorandum of Understanding with the State Oil Company of the Azerbaijan Republic giving it the exclusive right for a six month period, to negotiate the terms of the Rehabilitation, Exploration, Development and Production Sharing Agreement for the Neftchala field and associated block.

The Neftchala–Babazanan block, located in Azerbaijan's Lower Kura Depression is the largest onshore block in the country, covering approximately 2,500 sq. kms (625,000 acres) and containing three large tested structures located in the eastern half of the block as well as a number of smaller leads on the western portion.

The Neftchala field, located on the southeastern edge of the block on the shores of the Caspian Sea has been on production since 1931 and is the main producing structure on the block having produced approximately 48 million barrels of oil and 28 bcf of natural gas to date which accounts for only 42% of the recoverable reserves in place. The Neftchala and Hilli-Duzdag fields offer the potential for rehabilitation of existing wells as well as further development and exploration potential.

The 25 km long Babazanan-Durovdag structure, the largest and most northerly on the block was first drilled late in the 19th century and subsequently has been tested by approximately 40 additional wells over the years, most of which were drilled for shallow horizons. The deep potential of this structure offers an attractive exploratory upside for this project.

In the upcoming months, the Company will continue its technical evaluation of the block's potential as well as to negotiate on the terms of the new production sharing agreement.

Reserves

The Company's proved plus probable reserves increased significantly for the year with oil and NGLs up 31% and natural gas up 47% over the previous year. 80% of the Company's reserve base remains as proved.

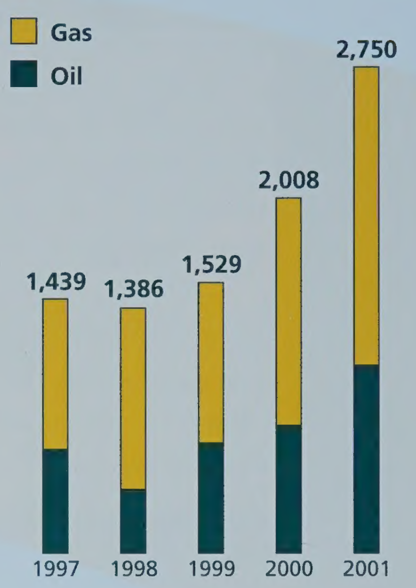
The product mix of the Company remains approximately balanced with oil and NGLs accounting for 61% of the reserves compared with 64% for the previous year. The Company's upcoming capital projects for the year are focused towards increasing gas production which will further equalize the reserve mix.

Based on the yearly average production rate, the Company's proved plus probable reserve life index for oil is 10 years. After adjusting for Clarke Lake production being restored, the reserve life index for the Company's proved plus probable gas reserves is 19 years, and 11 years based on total proved.

The table below presents the Company's proved plus probable reserves before royalties as evaluated by the independent firm of Chapman Petroleum Engineering Ltd. as at January 1, 2002.

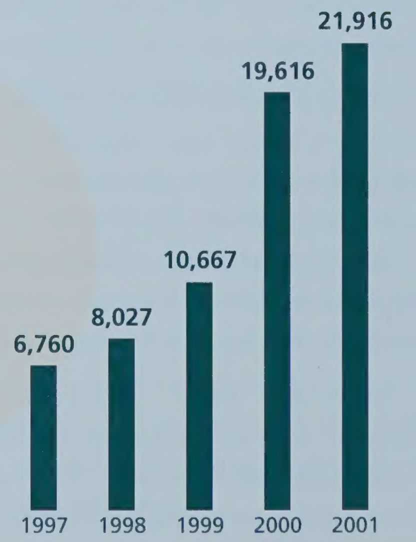
Proved + Probable Reserves

(MBOE, 6:1 Conversion)



Net Present Value

Proved + Probable Reserves
(10% DCF, $ Thousands)



Reserves

	Proved	Probable	Total
Gas (MMcf)	3,679	2,682	6,361
Oil (Mbbls)	1,515	54	1,569
NGLs (Mbbls)	76	45	121
Total (MBOE)	2,204	546	2,750

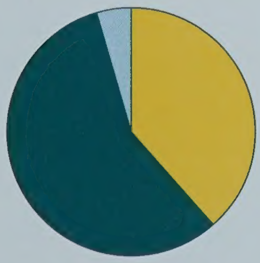
Pricing

	Crude Oil Edmonton Light Sweet ($ Cdn. per bbl)	
	Effective 1/1/02	Effective 1/1/01
2002	30.37	36.79
2003	34.22	37.89
2004	36.14	39.03
2005	38.06	40.21
2006	39.20	41.41
2007	40.38	42.65
2008	41.59	43.93
2009	42.84	45.25
2010	44.12	46.60
2011	45.45	48.00
2012	46.81	49.44

	Gas Reference Price ($ Cdn. per MMBTU)	
	Effective 1/1/02	Effective 1/1/01
2002	3.50	4.00
2003	3.75	4.12
2004	4.00	4.24
2005	4.00	4.37
2006	4.12	4.50
2007	4.24	4.64
2008	4.37	4.78
2009	4.50	4.92
2010	4.64	5.07
2011	4.78	5.22
2012	4.92	5.38

Reserve Allocation

(Proved + Probable)
(6:1 Conversion)



Gas	6,361 MMcf
Oil	1,569 Mbbls
NGLs	121 Mbbls
	2,750 MBOE

Production and Revenue

Revenues for the period were $4,527,950, a decrease of 4% over 2000. This was mainly the result of oil prices sharply declining during the fourth quarter combined with record light-heavy oil differentials during the same period. Average oil prices fell 34% from $32.20 in 2000 to $21.29 in 2001, while gas prices remained relatively constant at $5.74/Mcf in 2001 compared with $5.83/Mcf in 2000. Average daily production was 422 bopd and 596 Mcf/d as compared to 264 bopd and 748 Mcf/d in the prior year. Gas production was down from March 2001 onward due to a pipeline break at Clark Lake. This production is expected to be restored in April, 2002.

Royalties

Royalties, net of Alberta Royalty Tax Credit, increased 42% to $648,030 in 2001, up from $456,324 in 2000. This was largely due to Clarke Lake, B.C. royalty adjustments made in 2001, to production from the fourth quarter of 2000. Gas prices were at unprecedented highs during this time and the adjustments were therefore substantial. Also, in 2001, new Overriding and Freehold royalty obligations came due with a new well at Medicine River.

Operating Costs

Operating costs totaled $1,159,027 for the year which equates to $6.09 BOE, up 37% from $4.42 BOE in 2000. This increase is mainly attributed to non-operated costs from prior years being billed through in 2001 as well as power and fuel increases and increased repair costs.

General and Administrative

Total general and administrative expenses, net of recoveries, increased from $701,894 in 2000 to $801,383. This increase was due mainly to increased consulting services and increased shareholder service costs.

Interest

The 2001 interest expense of $23,655 was down significantly from $71,548 in 2000, due to a decrease in the average outstanding balance on the operating line of credit.

Depletion, Depreciation and Site Restoration

Total depletion, depreciation and site restoration provision was $1,074,732 as compared with $892,756 in 2000. This increase was due primarily to production increases throughout the year. The depletion rate per BOE in 2001 was $4.90 compared with $5.32 in 2000. These numbers reflect the 1Mcf = 6 BOE conversion equivalent.

Capital Expenditures

Total capital expenditures for the year were $1,562,240. This was spent primarily on operations consisting of drilling and completions, re-completions, workovers and abandonments and capitalized G&A.

Financial Position

At the end of the reporting period, International Sovereign had undrawn lines of credit of $4,405,000 on a $4,600,000 credit line.

Business Risks

The oil and gas industry is subject to numerous risks, including commodity prices, interest rate and exchange fluctuations, as well as environmental concerns and the success of future drilling. International Sovereign attempts to reduce and manage those risks which are controllable.

Safety and Environmental

Safety and environmental concerns are addressed through a corporate contingency plan and by continued emphasis on complying with environmental legislation.

Stock-Based Compensation and Other Stock-Based Payments

The Accounting Standards Board of the CICA has approved section 3870 "Stock-Based Compensation and Other Stock-Based Payments". Section 3870 establishes new standards for stock based compensation including the accounting related to the Company's Stock Option Plan. Management of the Company does not believe the adoption of the section will have a material impact on the financial statements.

Hedging Guidelines

In November 2001 the CICA issued Accounting Guideline 13 (AcG13), "Hedging Relationships", which will be effective for years beginning on or after July 1, 2002. AcG 13 addresses the identification, designation, documentation and effectiveness of hedging relationships for the purpose of applying hedge accounting. In addition, it deals with the discontinuance of hedge accounting and establishes conditions for applying hedge accounting. Under the new guidelines the Company is required to document its hedging relationship and explicitly demonstrate that the hedges are sufficiently effective in order to continue accrual accounting for positions hedged with derivatives. The Company believes that it will continue accrual accounting for hedges entered into for heavy oil pricing in the year 2002.

Management's Report

To the Shareholders of International Sovereign Energy Corp.

The information contained in this annual report and the accompanying financial statements and other financial information as well as the reporting process that produces such statements is the responsibility of Management.

Management maintains a system of internal controls designed to reasonably assure that transactions are appropriately authorized, that relevant and reliable financial information is produced in a timely manner and that the assets of the Corporation are adequately safeguarded.

The Management of the Company has the responsibility for the integrity and objectivity of the information contained in this annual report and to ensure that the operating information presented throughout this annual report is consistent with that shown in the financial statements, which are prepared by Management in accordance with generally accepted accounting principles.

The external auditors, appointed by the shareholders of the Company have examined the financial statements in order to provide an independent view as to the fairness of reported operating results and financial condition.

The Audit Committee of the Board of Directors which consists primarily of non-management directors have reviewed the financial statements including notes thereto, with Management and has reported to the Board of Directors.

The financial statements, upon the recommendation of the Audit Committee, have been approved by the Board of Directors.

Lutfur Rahman Khan
Chief Executive Officer

Don Campbell

Donald G. Campbell
Chief Operating Officer

Auditors' Report

To the Shareholders of International Sovereign Energy Corp.

We have audited the consolidated balance sheets of International Sovereign Energy Corp. (the "Company") as at December 31, 2001 and 2000 and the statements of operations and retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Calgary, Alberta
March 1, 2002

Consolidated Balance Sheets

December 31,	2001 $	2000 $
ASSETS		
Current		
Accounts receivable	**665,197**	799,226
Prepaid expenses and deposits	**6,800**	6,800
	671,997	806,026
Property and equipment (Note 3)	**10,076,369**	9,536,064
	10,748,366	10,342,090
LIABILITIES		
Current		
Bank indebtedness	**118,823**	364,817
Accounts payable and accrued liabilities	**580,949**	399,165
Operating loan (Note 4)	**195,000**	615,000
	894,772	1,378,982
Future income tax liability (Note 5)	**2,271,326**	1,895,157
Site restoration and abandonment provision	**204,366**	136,569
	3,370,464	3,410,708
SHAREHOLDERS' EQUITY		
Share capital (Note 6)	**6,234,734**	6,233,434
Retained earnings	**1,143,168**	697,948
	7,377,902	6,931,382
	10,748,366	10,342,090

Approved by the Board

Director

Director

Consolidated Statements of Operations and Retained Earnings

Years Ended December 31,	2001 $	2000 $
REVENUE		
Petroleum and natural gas revenues	**4,527,950**	4,706,765
Royalties, net of ARTC	**(648,030)**	(456,324)
Other income	**31,648**	16,177
	3,911,568	4,266,618
EXPENSES		
Operating costs	**1,159,027**	627,105
General and administrative	**801,383**	701,894
Interest	**23,655**	71,548
Depletion and depreciation	**1,006,935**	861,716
Site restoration	**67,797**	31,040
	3,058,797	2,293,303
Earnings Before Income Taxes	**852,771**	1,973,315
Income Taxes		
Current	**31,382**	250
Future (Note 5)	**376,169**	851,795
	407,551	852,045
Net Earnings (Note 8)	**445,220**	1,121,270
Retained Earnings (Deficit),		
Beginning of Year	**697,948**	(423,322)
Retained Earnings, End of Year	**1,143,168**	697,948

Consolidated Statements of Cash Flows

Years Ended December 31,	2001 $	2000 $
Cash Flows Related to the Following Activities:		
Operating		
Net earnings	**445,220**	1,121,270
Adjustments for:		
Depletion and depreciation	**1,006,935**	861,716
Site restoration	**67,797**	31,040
Future income taxes	**376,169**	851,795
Cash flow from operations (Note 8)	**1,896,121**	2,865,821
Changes in non-cash working capital	**315,813**	97,223
	2,211,934	2,963,044
Financing		
Decrease in operating loan	**(420,000)**	(213,000)
	(420,000)	(213,000)
Investing		
Additions to property and equipment	**(1,488,773)**	(3,081,824)
Site restoration costs	**(73,467)**	–
Proceeds on sale of property and equipment	**15,000**	–
Proceeds on exercise of stock options	**1,300**	–
	(1,545,940)	(3,081,824)
Net Increase (Decrease) in Cash and Cash Equivalents	**245,994**	(331,780)
Bank Indebtedness, Beginning of Year	**(364,817)**	(33,037)
Bank Indebtedness, End of Year	**(118,823)**	(364,817)

Years Ended December 31, 2001 and 2000

1 NATURE OF BUSINESS

International Sovereign Energy Corp., and its subsidiary (the "Company") is in the business of exploration for and development of petroleum and natural gas interests.

2 SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and practices.

Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary incorporated in Ecuador.

Cash and cash equivalents

Cash and cash equivalents include cash and short-term investments with a maturity of 90 days or less at the time of issue.

Property and equipment

The Company follows the full cost method of accounting for oil and gas operations as prescribed by the Canadian Institute of Chartered Accountants. All costs related to exploration and development of oil and gas reserves are capitalized. Such costs include lease acquisition costs, geological and geophysical expenses, carrying charges on non-producing properties, costs of drilling productive and non-productive wells and overhead charges related directly to acquisition, exploration and development activities.

Costs of acquiring and evaluating unproven properties are excluded initially from costs subject to depletion. These unproved properties are assessed regularly to ascertain whether impairment has occurred. When proven reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to the costs subject to depletion. Proceeds from disposal of properties will normally be applied as a reduction of the cost of the remaining assets unless the disposal represents a significant disposition of reserves, in which case a gain or loss will be recorded.

The net carrying value of the Company's petroleum and natural gas properties is limited to an ultimate recoverable amount. This is the aggregate of future net revenues from estimated proved reserves and the costs of unproved properties, net of impairment allowances, less future general and administrative costs, financing costs, site restoration and abandonment costs, and income taxes. Future net revenues are estimated using year-end prices and all costs are assumed to be constant.

For each cost center, the capitalized costs associated with proved reserves, including the costs of production equipment, are depleted and depreciated on the unit-of-production method based on the estimated proven reserves before royalties, determined by independent petroleum engineers. Oil and gas reserves and production are converted into equivalent units based upon estimated relative pricing content at a ratio of six thousand cubic feet of gas to one barrel of oil.

Site restoration and abandonment

The estimated cost for future site restoration and abandonment is provided on the unit-of-production method based on the estimated remaining proven reserves and is included in site restoration expense. Estimates are prepared by the Company's engineers based on current costs and regulations in effect at the balance sheet date. Actual site restoration and abandonment expenditures are charged to the accumulated provision account as incurred.

Revenue recognition

Petroleum and natural gas sales are recognized when the commodities are sold.

Joint venture accounting

A portion of the Company's exploration and production activities is conducted jointly with others and, accordingly, these consolidated financial statements reflect only the Company's proportionate interest in such activities.

Financial instruments

The carrying values of accounts receivable, accounts payable and accrued liabilities and operating loan approximate the fair value of these financial instruments due to the short-term maturity of these instruments.

Foreign currency translation

Transactions of the Company and its subsidiaries that are denominated in foreign currencies are recorded in Canadian dollars at exchange rates in effect at the related transaction dates. Assets and liabilities denominated in foreign currencies are adjusted to reflect exchange rates at the balance sheet date. Exchange gains and losses arising on the translation of monetary assets and liabilities are included in the determination of income for the year.

Stock based compensation plan

The Company has a stock based compensation plan, which is described in Note 6. No compensation expense is recognized for the plan when stock options are issued to employees. Any consideration paid by employees on exercise of stock options is credited to share capital. If stock options are repurchased from employees, the excess of the consideration paid over the carrying amount of the stock option cancelled is charged to retained earnings.

Future income taxes

The Company accounts for future income taxes using the liability method. Future income tax assets and liabilities are measured based upon temporary differences between the carrying values of assets and liabilities and their tax bases. Income tax expense (recovery) is computed based on the change during the year in the future tax assets and liabilities. Future income tax liabilities or assets are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse. Effects of changes in tax laws and tax rates are recognized when enacted.

Earnings per share

Basic earnings per common share is calculated using the weighted average number of common shares outstanding during the year. Diluted earnings per share is calculated on the basis of the weighted average number of shares outstanding during the year plus the additional common shares that would have been outstanding if potentially dilutive common shares had been issued using the "treasury stock" method.

Effective January 1, 2001, the Company retroactively adopted recommendations of the CICA Handbook Section 3500 regarding earnings per share. Under the revised standard, the treasury stock method is used instead of the imputed earnings approach for determining the dilutive effect of options issued. Prior to the adoption of the new recommendations, diluted per share amounts were determined using the imputed earnings method. If the imputed earnings method were utilized, diluted net earnings per common share would have been unchanged at $0.07 cents per share for the year (2000 - $0.16) and diluted cash flows from operations per common share would have been $0.28 for the year (2000 - $0.41).

PROPERTY AND EQUIPMENT

	2001 $	2000 $
Petroleum and natural gas properties	**13,716,232**	12,178,346
Furniture and equipment	**232,598**	223,244
	13,948,830	12,401,590
Less accumulated depletion and depreciation	**3,872,461**	2,865,526
	10,076,369	9,536,064

During the year, the Company capitalized general and administrative expenditures of $568,309 (2000 - $402,946) directly related to both Canadian and international exploration and development activities.

OPERATING LOAN

During the year, the Company secured a revolving line of credit to a maximum of $4,600,000. The operating loan bears interest at prime plus 0.75%. The operating loan is secured by a demand debenture for a minimum of $5,000,000, providing a floating charge over all assets of the Company, and a letter of undertaking not to encumber or dispose of assets, other than in the normal course of business, without consent of the Bank, and to provide security under section 426 of the Bank Act and/or assign natural gas contracts. At December 31, 2001, the balance outstanding with respect to this facility was $195,000 (2000 - $615,000). In addition, the lender has issued on behalf of the Company letters of credit totaling $7,500 (2000 - $189,000).

FUTURE INCOME TAXES

The provision for taxes varies from the amounts that would be computed by applying the effective Canadian federal and provincial income tax rates to earnings before taxes as shown below:

	2001 $	2000 $
Earnings before taxes	**852,771**	1,973,315
Corporate income tax rate	**42.62%**	44.62%
Computed income tax provision	**363,451**	880,493
Increase (decrease) resulting from:		
Non-deductible crown charges, net of ARTC	**238,501**	209,236
Taxable resource allowance	**23,011**	23,533
Resource allowance	**(73,710)**	(173,752)
Attributed Canadian royalty income	**(53,175)**	(90,944)
Non-deductible meals, entertainment and life insurance	**3,038**	2,034
Capital tax	**962**	250
Impact of changes in effective tax rate	**(77,288)**	–
Other	**(17,239)**	1,195
	407,551	852,045

The major components of the future income tax liability at December 31 using a combined federal and provincial rate of 42.62% (2000 - 44.62%) are as follows:

	Future Tax Liability **2001** **$**	2000 $
Taxable temporary differences:		
Carrying value in excess of tax basis	**2,426,720**	2,200,116
Non-capital losses	**–**	(169,804)
Attributed Canadian royalty income carryforward	**(132,384)**	(90,944)
Differences in capital cost allowance claim for resource Allowance	**(23,010)**	(44,211)
Balance, December 31	**2,271,326**	1,895,157

6. SHARE CAPITAL

	Number of Shares	Amount $
Authorized		
Unlimited number of Class A common voting shares		
Unlimited number of Class B common non-voting shares		
Unlimited number of Class A preferred voting, 7%, non-cumulative, redeemable shares		
Issued		
Class A common shares	6,442,713	6,233,434
Balance, December 31, 2000	6,442,713	6,233,434
Exercise of stock options	2,600	1,300
Balance, December 31, 2001	6,445,313	6,234,734

Stock option plan

Under the Company's stock option plan, the Company may grant options to its directors, officers and key employees to purchase Class A common shares ("Common Shares") from the Company at a fixed price not less than the fair market value of the stock on the day preceding the grant date. The Company has 644,272 common shares authorized for grants of options. The options would be exercisable equally over three years. The option's maximum term is five years.

	Options	Weighted Average Exercise Price $
As at December 31, 1999	355,667	0.75
Granted	494,667	0.50
Cancelled	(355,667)	0.75
As at December 31, 2000	494,667	0.50
Granted	–	–
Cancelled	(24,400)	0.50
Exercised	(2,600)	0.50
As at December 31, 2001	467,667	0.50
Exercisable at December 31, 2001	331,778	0.50

The following table summarizes information about stock options outstanding at December 31, 2001:

Range of Exercise Price(s) $	Options Outstanding at December 31, 2001	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price $	Exercisable at December 31, 2001	Weighted Average Exercise Price $
0.50	462,667	3.0	0.50	328,445	0.50
0.60	5,000	3.6	0.60	3,333	0.60
0.50 - 0.60	467,667			331,778	

7. RELATED PARTY TRANSACTIONS

During the year, the Company recovered general and administrative expenses totalling $24,000 (2000 - $24,000) from a corporation which has a director in common with the Company. At December 31, 2001, accounts payable of $30,992 (2000 - $13,633) include balances owing to a company which have a director in common with the Company. During the year, the Company paid $45,727 (2000 - $48,237) for legal services in the normal course of business to a law firm of which the partner is an officer of the Company. Transactions are determined at carrying amounts which approximates fair value.

8. EARNINGS AND CASH FLOWS FROM OPERATIONS PER COMMON SHARE

	2001	2000
Earnings per common share		
Basic	**$ 0.07**	$ 0.17
Diluted	**$ 0.07**	$ 0.17
Cash flows from operations per common share		
Basic	**$ 0.29**	$ 0.44
Diluted	**$ 0.29**	$ 0.44
Weighted average number of common shares		
Basic	**6,445,142**	6,442,713
Diluted	**6,578,047**	6,542,338

9. COMMITMENT

The Company has committed to a lease for premises expiring in August of 2006. The minimum annual payment required on the lease is $62,171.

10. SEGMENTED INFORMATION

The Company sells its petroleum and natural gas products to various purchasers. For 2001, two large integrated purchasers accounted for 56% and 14% (2000 - 30%, 15% and 10%) of the Company's gross revenues.

The Company's core area of operation is in Canada. The Company is currently investigating opportunities in other countries. Total costs spent in 2001: $529,135 (2000 - $371,720).

11. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform to the presentation adopted for current year.

12. SUPPLEMENTARY CASH FLOW INFORMATION

	2001 $	2000 $
Cash taxes paid	**501**	250
Cash interest paid	**23,655**	71,548

Corporate Information

Lutfur Rahman Khan
Chairman of the Board and Chief Executive Officer

Donald G. Campbell
Sr. Vice President Engineering & Production and Chief Operating Officer

George P. Bowley
Sr. Vice President Exploration & Development

Dr. Waseem Rahman
Sr. Vice President Administration

Omair Choudhry
Vice President Personnel & Finance

Timothy S. Hoar
Corporate Secretary & General Counsel

Directors

Lutfur Rahman Khan (2*) (3*)

Dr. Asif Ali Syed (1*)

Omair Choudhry (2)

Donald G. Campbell (3)

Dr. Waseem Rahman (1) (3)

Arman Aziz (1) (2)

(1) Member of the Audit Committee
(2) Member of the Compensation Committee
(3) Member of the Executive Committee
* Chairman

Officers

Lutfur Rahman Khan
Chairman, President and Chief Executive Officer

Donald G. Campbell
Sr. Vice President Engineering & Production and Chief Operating Officer

George P. Bowley
Sr. Vice President Exploration & Development

Dr. Waseem Rahman
Sr. Vice President Administration

Nadeem R. Khan
Sr. Vice President Business Development

Omair Choudhry
Vice President Personnel & Finance

Timothy S. Hoar
Corporate Secretary & General Counsel

Corporate Directory

Vancouver Executive Office
502 - 815 Hornby Street
Vancouver, BC
Canada V6Z 2E6

Tel: (604) 684-7372
Fax: (604) 684-2407

Calgary Operations Office
1750, 801 - 6th Avenue S.W.
Calgary, AB
Canada T2P 3W2

Tel: (403) 263-2472
Fax: (403) 264-7035

Overseas Office
No. 17 Street 37
Sector F-8/1
Islamabad, Pakistan

Tel: 011-92-51-2280 455
Fax: 011-92-51-2260 698

Registrar and Transfer Agent

Valiant Trust Company
Calgary, AB

Banker

The Bank of Nova Scotia
Calgary, AB

Auditors

Deloitte & Touche LLP
Calgary, AB

Independent Engineers

Chapman Petroleum Engineering Ltd.
Calgary, AB

Legal Counsel

ProVenture Law
Calgary, AB

Stock Exchange Listing

Canadian Venture Exchange
Symbol "ISR"

International
Sovereign Energy Corp.

Executive Office
502 - 815 Hornby Street
Vancouver, BC
Canada V6Z 2E6

Operations Office
1750, 801 - 6th Avenue S.W.
Calgary, AB
Canada T2P 3W2

www.internationalsovereign.com